

Message Text

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STADIS////////////////////////////////////

E.O. 11652: N/A

TAGS: EINV, MA, US

SUBJECT: N-REN FERTILIZER PLANT PROJECT

REF: A) 77 ANTANANARIVO 2333, B) STATE 77055

SUMMARY AND ACTION REQUESTED: EXIM BANK STAFF HAS RECOMMENDED DENIAL OF N-REN'S REQUEST FOR PRELIMINARY COMMITMENT ON CREDIT TO FINANCE US COSTS OF ZE-REN FERTILIZER COMPLEX. DEPARTMENT HAS OBTAINED ONE WEEK DELAY IN EXIM BOARD CONSIDERATION OF CASE, UNTIL THURSDAY, APRIL 13, BUT NEEDS EMBASSY INPUTS BY COB APRIL 10 TO HELP SUPPORT N-REN'S CASE. END SUMMARY

I. IN EXIM STAFF PAPER, PREPARED FOR APRIL 6 BOARD
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MEETING, STAFF RECOMMENDED DENIAL BECAUSE: "THE INSUFFICIENT MARKET FOR FERTILIZER, THE HIGH CAPITAL COSTS OF THIS PROJECT, THE LACK OF ADEQUATE EXTENSION SERVICES AND THE ABSENCE OF A COORDINATED AGRICULTURAL POLICY ON THE PART OF THE GOM LEAD TO THE CONCLUSION THAT THE PROJECT IS NOT CREDITWORTHY ON ITS OWN MERITS. THE ALTERNATIVE WOULD BE TO CONSIDER A LOAN DIRECTLY TO THE GOM. HOWEVER, THE

FINANCIAL POSITION OF THAT GOVERNMENT IS NOT STRONG."

2. EXIM STAFF NOTES "THE FINANCIAL VIABILITY OF THE PROJECT IS PREDICATED UPON THE EXPECTED PRODUCTION OF UREA FERTILIZER MAINLY TO SERVE THE DOMESTIC MARKET. THE CASH FLOW PROJECTIONS PREPARED BY N-REN AND SUBMITTED TO EXIMBANK ARE BASED UPON EXPECTED ANNUAL SALES VOLUME OF 90,000 METRIC TONS WHICH THE STAFF CONSIDERS EXCESSIVE...."

3. STAFF'S CASH FLOW PROJECTIONS ARE PREPARED ON TWO BASES -- ANNUAL VOLUME OF 5500 METRIC TONS, THE HISTORICAL AVERAGE IMPORT LEVEL, AND ANNUAL VOLUME OF 45,000 METRIC TONS, WHICH IS THE AMOUNT THE GDRM WOULD COMMIT ITSELF TO PURCHASE UNDER THE DEAL. EVEN AT THE HIGHER LEVEL, NET CASH FLOW AS COMPUTED IS NEGATIVE THROUGH 1984, WHICH EXIM STAFF ARGUES IS BY ITSELF SUFFICIENT GROUND FOR DENIAL.

4. STAFF ADDS TWO OTHER CONSIDERATIONS. CITING WORLD BANK AGRICULTURAL ECONOMIST JUST RETURNED FROM MADAGASCAR, IT ARGUES THAT EXTENSION SERVICES ARE LACKING IN MADAGASCAR; GOVERNMENT AT THIS TIME IS "NOT MAKING ANY EFFORTS TO PROVIDE FOR SUCH SERVICES"; AND WITHOUT THEM FERTILIZER THAT THE GDRM PROPOSES TO BUY COULD NOT BE USED. IMPLICIT IN THIS ARGUMENT IS THE BELIEF THAT GDRM COMMITMENT TO PURCHASE FERTILIZER WOULD NOT BE CARRIED OUT, PUTTING THE PROJECT EVEN DEEPER INTO THE RED.
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5. STAFF ALSO RAISES DOUBTS ABOUT WHETHER INCREASED FERTILIZER AVAILABILITY WOULD INCREASE RICE PRODUCTION. IT ACKNOWLEDGES THAT DOMESTIC SUBSTITUTIONS FOR FERTILIZER AND RICE IMPORTS COULD BE REGARDED AS FOREIGN EXCHANGE BENEFIT INDIRECTLY ATTRIBUTABLE TO THIS PROJECT (THIS BENEFIT IS NOT INCLUDED IN CASH FLOW PROJECTION, WHICH IS TECHNICALLY CORRECT BUT GIVES AN UNWARRANTEDLY PESSIMISTIC IMPRESSION OF THE FINANCIAL PROSPECTS). THE SAME WORLD BANK ECONOMIST SAYS, HOWEVER, THAT EFFORTS TO INCREASE RICE PRODUCTION IN MADAGASCAR HAVE BEEN STYMIED NOT BY LACK OF FERTILIZER BUT BECAUSE OF "UN SOUND GOVERNMENT PRICING POLICIES, ADVERSE WEATHER CONDITIONS AND WEAK TRANSPORTATION AND MARKETING SERVICES."

6. EXIM STAFF REPORT ALSO SHRUGS OFF POSSIBILITY OF EXPORTING ANY OF THE SURPLUS PRODUCTION FROM THE PROPOSED COMPLEX, ALTHOUGH PROJECTED MAJOR AGRICULTURAL EXPANSIONS IN ZAMBIA, MALAWI AND TANZANIA RAISE AT LEAST THE POSSIBILITY OF SIGNIFICANT EXPORT MARKETS IN THE NEAR FUTURE. DEPARTMENT BELIEVES THAT THESE PROSPECTS AT LEAST DESERVE ANALYTICAL CONSIDERATION AND SOME MENTION IN CASH FLOW

PROJECTIONS.

7. AS POST IS AWARE, EXIM HAS IN THE PAST FINANCED

PROJECTS WHERE IT HAD DOUBTS ABOUT THEIR VIABILITY, BUT WHERE GOVERNMENT GUARANTEE AND GOVERNMENT'S OWN CREDIT-WORTHINESS WERE SUFFICIENT TO GIVE REASONABLE ASSURANCE OF REPAYMENT. IN THIS CASE, HOWEVER, STAFF SAID THAT " THE CONCLUSION CAN BE DRAWN THAT, WHILE ITS EXISTING DEBT IS LOW AND OF A VERY CONCESSIONAL NATURE, THEREBY RESULTING IN A LOW DEBT SERVICING BURDEN OF SOME 4 TO 5 PERCENT OF EXPORT EARNINGS, THE COUNTRY'S ABILITY TO SERVICE NEW DEBT IS RATHER LIMITED BECAUSE OF ITS GENERAL POVERTY. EXTERNAL FINANCING ON COMMERCIAL TERMS OF ANY SIZE IS LIMITED OFFICIAL USE

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PRUDENTLY FEASIBLE ONLY FOR INVESTMENTS WHICH GENERATE SUFFICIENT FOREIGN EXCHANGE EARNINGS TO SERVICE THE NEW DEBT."

8. FINALLY, ALTHOUGH IT IS NOT DISCUSSED IN THE REPORT, EXIM STAFF HAS MISGIVINGS ABOUT N-REN'S ABILITY TO EXECUTE THE PROJECT, BASED ON REPORTS OF SERIOUS PROBLEMS IN GABON AND KENYA. FYI: IN EXIM BOARD MEETING POINT WAS MADE THAT FIRM SHOULD HAVE THE CHANCE TO RESPOND TO EXIM'S DOUBTS IN THIS REGARD. END FYI. DEPARTMENT NOTES ALSO THAT THERE ARE NO INDICATIONS OF PROBLEMS WITH PROJECT IN SUDAN, ABOUT WHICH EMBASSY KHARTOUM IS ENTHUSIASTIC, OR WITH PLANT IN MAURITIUS. WE ARE ALSO UNAWARE OF PROBLEMS WITH FIRM'S OPERATIONS ON OTHER CONTINENTS. IN ANY CASE, DEPARTMENT IS SEEKING OTHER INDEPENDENT JUDGMENTS OF FIRM'S CAPABILITIES AND RELIABILITY, FOR PRESENTATION TO EXIM BOARD.

9. ACTION REQUESTED: DEPARTMENT NEEDS, BEFORE COB MONDAY APRIL 10, WHATEVER INFORMATION OR ANALYSIS EMBASSY CAN BRING TO BEAR , BUT PARTICULARLY:

A) ANY PLANS GDRM MAY HAVE TO IMPROVE EXTENSION SERVICES (INCLUDING RURAL INFRASTRUCTURE, AGRICULTURAL EDUCATION, IRRIGATION, ETC.) WHICH WOULD ENABLE ECONOMIC USE OF ITS SHARE OF PLANT'S UREA OUTPUT;

B) ANY GDRM PLANS TO MODIFY PRICING POLICIES OR TAKE OTHER ACTIONS (IMPROVED MARKETING, MORE LIBERAL AGRICULTURAL CREDIT, ETC.) TO ENCOURAGE FARMERS TO GROW MORE RICE (IN THIS CONNECTION, WE NOTE THAT THE WORLD BANK HAS SEVEN PROJECTS IN THE PIPELINE IN MADAGASCAR, INCLUDING ONES IN RURAL INFRASTRUCTURE AND IRRIGATION; WORLD BANK CUSTOMAR-LIMITED OFFICIAL USE

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ILY ADVISES BORROWERS ON POLICIES WHICH IT FEELS IMPACT
ADVERSELY ON DEVELOPMENT, PARTICULARLY IN SECTORS WHERE IT
IS INVOLVED);

C) CREDITWORTHINESS OF MADAGASCAR GOVERNMENT, INCLUDING

PAYMENT RECORD ON PRESENT AND PAST OBLIGATIONS, QUALITY OF
GOVERNMENT PERFORMANCE ON BUDGETING AND ECONOMIC PLANNING,
AND ANYTHING ELSE THAT ARGUES AGAINST NEGATIVE CONCLUSION
ON GDRM CREDITWORTHINESS RECOUNTED IN PARA 7 ABOVE;

D) ESTIMATES OF THE IMPACT, POSITIVE AND NEGATIVE, OF
ALTERNATIVE EXIM BANK DECISIONS, GIVEN THAT CANADIAN,
AUSTRIAN AND BELGIAN EXPORT CREDIT AGENCIES HAVE ALL
INDICATED READINESS TO PARTICIPATE. WHAT WOULD EFFECT BE
ON US ACCESS TO THE MALAGASY MARKET? ON BILATERAL RELA-
TIONS? VANCE

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